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Report of the Director of the Office of Audit and Investigation Services on UNFPA internal audit and investigation activities in 2016

Opinion on the Adequacy and Effectiveness of the UNFPA Framework of Governance, Risk Management and Control

In the opinion of the Director of the Office of Audit and Investigation Services, based on the scope of work undertaken, the adequacy and effectiveness of the UNFPA governance, risk management and internal control processes was 'partially satisfactory' – which means that the processes were generally established and functioning but one or more issues were identified that, if not addressed by management, could negatively affect the achievement of UNFPA objectives. None of the issues identified were, however, assessed as having the potential to seriously compromise that achievement.

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I. Opinion

1. The opinion on the adequacy and effectiveness of the UNFPA Framework of Governance, Risk Management and Control is provided in accordance with Executive Board decision 2015/13 of June 2015.

2. In the opinion of the Director of the Office of Audit and Investigation Services (OAIS), based on the scope of work undertaken, the adequacy and effectiveness of the UNFPA governance, risk management and internal control processes was 'partially satisfactory' – which means that the processes were generally established and functioning but one or more issues were identified that, if not addressed by management, could negatively affect the achievement of UNFPA objectives. None of the issues identified were, however, assessed as having the potential to seriously compromise that achievement.

II. UNFPA management responsibilities

3. UNFPA management is responsible for designing and maintaining the governance, risk management and internal control processes and ensuring that these operate effectively. The responsibility of OAIS is limited to independently assess the adequacy and effectiveness of these processes.

III. Criteria used for assessing the adequacy and effectiveness of the governance, risk management and internal control processes

4. OAIS utilized the 2013 internal control framework and the 2014 enterprise risk management integrated framework of the Committee of Sponsoring Organizations of the Treadway Commission – adopted by UNFPA as the basis for its internal control framework and enterprise risk management process, respectively – as the main criteria for assessing the adequacy and effectiveness of the governance, risk management and internal control processes to provide reasonable assurance on the achievement of the UNFPA objectives in the following categories:

(a) Strategy: fulfilment of UNFPA mandate and achievement of its strategic plan goals;

(b) Operations: effectiveness and efficiency of UNFPA operations, including (i) operational and financial performance goals; (ii) conformity of expenses with the purpose for which funds were allocated; and (iii) safeguarding of assets against loss;

(c) Reporting: reliability of internal and external (i) financial reporting and (ii) non-financial reporting by UNFPA; and

(d) Compliance: adherence to the UNFPA regulatory framework, as established in its legislative mandate, rules, regulations, policies and procedures.

IV. Scope of audit work and additional sources of evidence considered for formulating the opinion

5. The opinion is based on (a) OAIS audits of country offices, regional offices, core business processes, programmes, and information and communications technology components; and (b) joint audits of joint United Nations activities, concluded between 1 January and 31 December 2016, as detailed in the Report of the Director of the Office of Audit and Investigation Services on UNFPA internal audit and investigation activities in 2016 (DP/FPA/2017/6, sections IV and VI, and Annex 2).

6. All OAIS audits were conducted in accordance with the applicable policies by which it has to abide – the oversight policy, the financial rules and regulations, the staff rules and regulations, and the International Standards for the Professional Practice of Internal Auditing.[1]

7. To formulate its opinion, OAIS considered, as appropriate, other sources of evidence, including: (a) cumulative audit knowledge stemming from OAIS audits completed in previous years, as considered relevant; (b) the outcome of the 2016 audit risk assessment, undertaken to support the development of the 2017 audit plan; (c) the status of implementation of internal audit recommendations as at 31 December 2016; (d) systemic issues noted by investigations completed in 2016; (e) audit findings reported by the United Nations Board of Auditors in its management letter on the interim 2016 audit of UNFPA, dated 30 January 2017; (f) results of national execution audits commissioned by management and completed in 2016; (g) results of control self-assessments completed by numerous country and regional offices as well as certain headquarters business units in January 2017; (h) third-party assurance reports obtained by management regarding outsourced vendor management, and messaging and collaboration systems hosting and management services; and (i) results of the strategic and fraud risk assessments completed as part of the enterprise risk management process under implementation by management.

8. The audits and some additional sources of evidence considered for purposes of formulating the opinion refer to activities undertaken by UNFPA primarily in 2015 or in previous years. Additional matters could have been identified that may have impacted the opinion had additional audit work been performed in 2016 and/or in previous years.

9. In 2016, as in previous years, UNFPA outsourced significant functions to other United Nations system organizations, including: (a) selected human resources management activities; (b) staff and service contract holder payroll preparation and payment; (c) payment processing; (d) treasury management; and (e) hosting and management of the enterprise resource planning system. UNFPA management relied on the management and fiduciary oversight activities undertaken by the organizations to which these functions were outsourced, as regards the adequacy and effectiveness of the related governance, risk management and internal control processes. These are not covered by the OAIS opinion.

10. In addition, UNFPA outsources significant information and communications technology functions, including the hosting of significant systems, to third-party service providers. UNFPA management did not obtain third-party assurance reports on the adequacy and effectiveness of the governance, risk management and internal control processes related to firewall and vulnerability management, technology infrastructure maintenance and website hosting services; these are not covered by the OAIS opinion.

V. Process followed for aggregating audit results and assessing issues

11. Results of the audits undertaken by OAIS and additional evidence considered to formulate the opinion were aggregated by audit area and process, using the framework previously developed for the audit risk assessment and for reporting key findings of internal audit and investigation activities.

[1] Promulgated by the Institute of Internal Auditors (IIA).

12. The potential impact of the issues identified on the achievement of the relevant UNFPA objectives in the categories detailed in paragraph 4 above was assessed taking in consideration: (a) the ratings assigned to the entities, processes, programmes and areas covered by the audits, weighted based on the value of audited expenses; (b) the nature and materiality of the issues identified, individually and in the aggregate; (c) their root cause and pervasiveness; (d) the risk profile, as determined based on the outcome of the OAIS audit risk assessment, and the materiality of the processes affected; (e) the degree to which internal audit recommendations related to these processes had been implemented; and (f) the adequacy and effectiveness of compensating controls operating at headquarters or at regional office level that could contribute to mitigating the impact of the issues found.

VI. Basis for the opinion formulated

13. OAIS assessed the adequacy and effectiveness of the UNFPA governance, risk management and internal control processes as 'partially satisfactory' – which means that these processes were generally functioning but that one or more issues were identified that, if not addressed by management, could negatively affect the achievement in the categories detailed in paragraph 4 above.

14. The key improvement areas leading to this opinion are described below:

A. Governance and risk management

Integrated control framework

15. The development of the comprehensive and integrated control framework should be finalized, covering all relevant governance, programme and operations management processes – including information and communications technology; and clearly outlining the key controls required to minimize risks identified for each process, the related implementation steps and the responsibility for operating them.

16. Completion of such a framework will provide a useful tool to allow management to enhance awareness about, and training on, internal control requirements (supplementing efforts already under way, such as a periodic control self-assessment survey); better enforce accountability for internal controls; and more promptly and effectively complete the planned review and update of the policies and procedures manual, under way at the time of developing the present opinion.

Enterprise risk management

17. Changes to the enterprise risk management process were introduced in 2016, particularly in the functionality of '*myRisks*', the 'strategic information system' module developed to document strategic and fraud risk assessments undertaken by field offices and headquarters units.

18. The process needs to mature further, improving on its design and operating effectiveness, bridging the skill-set gaps that limit the relevance of assessments completed by business units. The activities planned for the risk response phase should be fully implemented, including the review and analysis by the risk treatment working groups (i.e., groups of subject matter experts) planned for the second quarter of 2017.

19. Management plans to introduce further enhancements to the process are welcomed, including the use of a differentiated risk management approach for countries operating in humanitarian and fragile contexts or facing large increases in programme size, the issuance of a revised fraud policy, and fraud awareness training for the UNFPA personnel and implementing partners.

Organizational structure and staffing

(i) Business unit capacity

20. Timelier approval and implementation of business unit organizational structure and personnel alignment reviews, typically undertaken concurrently with the development of new programmes or in response to significant programme changes, is needed to ensure that capabilities remain aligned to programme delivery and operational needs.

(ii) Vacancies in key management positions

21. Management took action to lower the vacancy rate for key positions, such as the leadership pool implementation. Audits continued nevertheless to reveal instances of offices delivering large and/or complex programmes, or operating in fragile contexts, where key vacancies were not promptly filled – depriving these offices from sustained leadership and management oversight.

Headquarters and regional office support and oversight

22. Managerial oversight controls (i.e., "second line of defense") at headquarters and regional offices should be strengthened – defining clear terms of reference and guidelines as regards the nature, scope and frequency of management oversight; develop appropriate managerial reports; and assign sufficient human and financial resources thereto.

23. To minimize the risk arising from gaps in management leadership and oversight, headquarters and regional office support to, and oversight over, business units affected by prolonged vacancies should be increased until such time as the positions are filled.

B. Internal Control

Programme Management

(i) Programme planning and implementation

a. Results-based management

24. More comprehensive programme results and resources frameworks should be developed, supplementing country, regional and corporate programme documents. They should better outline: (a) programme outputs; (b) indicators and related baselines and targets; (c) milestones (i.e., intermediate results); and (d) resource estimates, with disaggregated information for all periods within the programme cycle. This would allow a more effective planning and implementation of programme activities and better racking of progress towards achieving expected programme results.

25. This need is particularly important for offices operating in 'delivering as one' countries that decided to use joint programme instruments, such as the United Nations Development Assistance Framework or the United Nations Development Assistance Plan, results and resources matrices, as these often provide information insufficiently detailed for programme planning and results tracking.

26. Challenges in this area are exacerbated by limited quality assurance at regional office level.

27. Management indicated that it is considering mandating the use of new programme instruments, such as project or output documents, to help ensure more effective programme planning and implementation, as well as tracking of programme results.

b. Workplan management

28. Improvements in workplan management were noted, following the implementation, in November 2014, of the global programming system, particularly as regards workplan set-up in the Atlas application and increased visibility and transparency on workplan activities and related budgets. Improvements were also fostered by workplan reviews undertaken by the programme division, the results of which were widely disseminated with country and regional offices.

29. The process should be further improved, particularly as regards: (a) the timeliness of workplan finalization and their level of details; (b) their regular updates, to reflect significant changes to planned activities, budgets or resources; (c) better rationalization and documentation of workplan budgets; and (d) better alignment of the signed workplans with those included in the global programming system workplan 'snapshots'.

30. The overall effectiveness of the workplan management process should be further strengthened, remedying deficiencies in the design of global programming application controls in the areas of (a) access to global programming system functions; (b) segregation of duties between workplan development and maintenance processes; (c) workplan budget development and approval; and (d) workplan generation and approval.

c. Programme financial management controls

31. Programme financial management procedures and controls require further strengthening, with a rigour similar to that currently applied over the institutional budget, including the development of detailed and supported workplan budgets, by expense category; periodic review of expenses incurred; and regular budget-to-actual reconciliations, by activity and expense category. Enhanced controls should also be applied to ensure appropriate costing of funding proposals, project documents and workplans, to reflect all direct and indirect costs necessary to implement the related activities, and address the cross-subsidization of core resources and programme activities funded from non-core resources.

d. Humanitarian response

32. Improvements as regards humanitarian response activities were noted in 2016. Further actions are required to address programme and operational bottlenecks and enhance the UNFPA performance in this area. This includes the implementation of the funding mechanisms mandated by the Executive Board to bridge funding shortfalls; access to flexible funding to sustain response efforts; and enhancing surge capability and alignment of human resource capacity, to ensure timelier and more effective delivery in humanitarian contexts.

(ii) National execution

a. *Implementing partner capacity*

33. The capacity assessments reviewed in 2016 were undertaken primarily in 2015 or previous years. They continued to reveal the need for a more thorough and better documented assessment of the programmatic and financial management capacity of implementing partners, including their fraud prevention controls, particularly in humanitarian and fragile contexts. Improvement opportunities were also identified by the Board of Auditors in its 2017 management letter.

34. It should be remembered that the revised harmonized approach to cash transfers (HACT) framework was rolled out in 2016; hence, the audits concluded in 2016 partially reflect this change, and the improvements expected therefrom.

b. Financial monitoring of implementing partners

35. Enhanced financial monitoring of implementing partners, to ensure that funds provided are used for their intended purposes in line with the approved workplans and budgets, is an area needing continuous attention.

36. As mentioned in paragraph 34, improvements from the roll-out, in 2016, of the revised harmonized approach to cash transfers (HACT) framework have yet to be fully in place.

(iii) Supply-chain management

37. As mentioned in the past, increased support to programme countries, together with other relevant programme stakeholders, to address gaps in supply-chain management systems that may reduce availability of reproductive health commodities and originate stock-outs is required. Receiving and inspection controls should be more consistently performed and documented. Regular monitoring of inventory of reproductive health commodities held by implementing partners, as well as tracking its timely distribution and availability at service delivery points, continues to be needed.

38. To effectively address the above requires the implementation of more effective and integrated supply-chain management organizational arrangements, processes and systems, from procurement to the 'last mile'. Enhanced quantification, planning, sourcing, procurement, delivery and distribution of reproductive health commodities should support improved achievement of programme goals; foster enhanced cost-effectiveness; and help discharge better fiduciary oversight and contractual obligations.

Operations Management

(i) Human resources management

39. Improvements were noted in the management of personnel engaged under service contracts, particularly as regards their compensation (now managed through the payroll system – which also provides increased transparency on the number of service contract holders) and performance planning and assessment (now managed through the performance assessment and development system). Other activities, such as contract issuance, continued to be managed manually, and some level of deviation from the requirements of the 2014 policy on service contracts was noted on several occasions.

40. More limited progress was made as regards individual consultancy contracts. A tool was developed to register individual consultancy contracts, to be rolled out globally as from 2017, albeit with limited integration with the ERP system. Contract award and consultancy fee calculation and payment continue to be managed manually, and some level of deviation from the requirements of the 2015 policy on individual consultants was observed.

41. Further, limited integration of the corporate and regional consultant rosters, for both service contracts and individual consultants, was noted.

(ii) Procurement

42. Procurement procedures are adequately designed and operate effectively for procurement activities undertaken by the procurement services branch, which account for

approximately half of total procurement at UNFPA. Instances of non-compliance with procurement procedures were found on several occasions at country office level, particularly as regards tendering and contract award.

43. 'Second line of defense' controls under implementation at the end of 2016 need to be strengthened to address the risks originating from the above.

(iii) Financial management

44. Multiple instances of expenses miscoded in account codes, were found – which diminishes the overall reliability of programme and financial information. Compensating controls implemented by headquarters as part of the financial statement preparation process partially mitigate the impact of this issue for financial reporting purposes.

45. To minimize the risks of transactions executed without appropriate management approval and, potentially, incurring expenses in excess of available financial resources, financial commitments should be more timely reflected and approved in Atlas, through issuance of requisitions or purchase orders prior to decisions to procure goods and services or reimburse expenses are communicated to vendors or implementing partners.

(iv) Information and communication technology

46. The governance of information and communications technology projects should be enhanced to ensure that new systems which are rolled out incorporate adequately designed access and other application controls, and enforce segregation of duties requirements.

47. Management proactive efforts in strengthening information and communication technology were noted.